Supreme Court of the United States.

October Term, 1897.

No. 321.

OSCAR R. LOOKER, CHARLES A. KENT, WILLIAM S. GREEN, *et al.*
Plaintiffs in Error,
vs.
FRED A. MAYNARD, Attorney General of the State of Michigan, on the relation of JOSEPH W. DUSENBURY and WILL. J. DUSENBURY.

In Error to the Supreme Court of the State of Michigan.

BRIEF FOR PLAINTIFFS IN ERROR.

STATEMENT OF THE CASE.

This court is asked to review the judgment of the Supreme Court of Michigan. The only federal question

involved is, whether or not the judgment of the state court enforces a state statute which, as construed, is in conflict with the constitution of the United States.

The Attorney General of Michigan filed in the state supreme court an information to try the title of plaintiffs in error to the position of directors in the Michigan Mutual Life Insurance Company.

This company was organized July 3, 1870, under an act for the formation of life insurance companies, approved March 30, 1869, and constituting chapter 131 of Howell's Annotated Statutes.

Section 2 of said act provides: "The persons so associating shall subscribe articles of association which shall contain," (paragraph 4,) "The manner in which the corporate powers are to be exercised, the number of directors, and other officers, and the manner of electing the same, and how many of the directors shall constitute a quorum, and the manner of filling vacancies;" and in paragraph 7, "Any terms and conditions of membership therein which the corporators may have agreed upon, and which they may deem important to have set forth in said articles."

Section 5 of said act provides: "The articles of association shall be submitted to the attorney general for his examination, and if found by him to be in compliance with this act, he shall so certify to the secretary of state." All the requirements of this act were complied with, and the company has been doing business ever since. Said articles of association contain the following: "The corporate powers of the company shall be exercised by a board of directors, which shall consist of twenty-one members, which may be increased at the option of the board to not more than forty. The first meeting for the election of directors shall be called by the present officers, and held as soon as possible after these articles take effect. No person shall be eligible who is not the owner of at least ten

shares of the guarantee capital of the company, and at least two-thirds of the directors shall be residents of the state of Michigan. The board at their first meeting shall divide themselves by lot into three equal classes, as near as may be, whose terms of office shall expire at the end of one, two and three years respectively, and thereafter one-third of the directors shall be chosen annually for the class, whose term then expires, who shall hold office for three years, or until their successors are elected. The election of directors shall be had at the annual meeting of the company, which shall be held on the last Tuesday in January, at the office of the company in Detroit. They shall be chosen by ballot, and a majority of the votes cast shall elect. Every shareholder shall be entitled to one vote for directors for every share of guarantee capital standing in his name on the books of the company, and may vote in person or by proxy, and every policy holder insured in this company for the period of his natural life, in the sum of not less than five thousand dollars, shall also be entitled to one vote in the annual election of directors which vote must be given in person."

Directors have always been elected in accordance with these provisions.

In 1885, the legislature of Michigan passed an act entitled "An act to secure the minority of stockholders in corporations, organized under general laws, the power of electing a representative membership in boards of directors." Section 1, reads: "The people of the state of Michigan enact: That in all elections for directors of any corporation organized under any general law of this state other than municipal, every stockholder shall have the right to vote in person or by proxy the number of shares of stock owned by him for as many persons as there may be directors elected, or to cumulate said shares and give one candidate as many votes as equal the number of directors

multiplied by the number of shares of his stock, or to distribute them on the same principles among as many candidates as he shall think fit. All such corporations shall elect their directors annually, and the entire number of directors shall be balloted for at one time, and not separately."

The constitution of Michigan, adopted in 1850, contains the following: "Corporations may be formed under general laws, but shall not be created by special act except for municipal purposes; all laws passed pursuant to this section, may be amended, altered or repealed."

At the annual election of directors, January 28, 1896, relator J. W. Dusenbury, undertook to vote his stock according to said minority law. He voted for himself and relator Will J. Dusenbury. If his claim had been allowed, each of relators would have had 5571 votes, and would have been elected. His claim was rejected, and the votes were counted according to the articles of association, and in accordance therewith, all of respondent's, nine in number, were declared elected for a term of three years.

The judgment of the Supreme Court of Michigan was, that respondents be all ousted from office as directors of the Michigan Mutual Life Insurance Company, and that relators were elected, and will hold office until their successors are elected. The respondents claim that this judgment deprives them of rights secured by the constitution of the United States. The provisions relied on are, that, forbidding states to pass laws impairing the obligation of contracts and that against taking property without due process of law.

I.

The articles of association of the Michigan Mutual Life Insurance Company as to the method of electing directors constituted a legal contract between the original stockholders, binding on their successors, protected by the constitution of the United States against State interference, except so far as the power to change the contract, has been reserved.

1. The persons associating are not merely permitted, they are required to put in their articles of association, "The manner in which the corporate powers are to be exercised, the number of directors and other officers, and the manner of electing the same, and how many directors shall constitute a quorum, and the manner of filling all vacancies."

These things had to be determined by agreement before put in the articles. The agreement must have been that of the persons associating. It is sometimes said that the articles of association are an agreement of the persons associating with the corporation, but this seems inaccurate. How can a corporation make an agreement before it has begun to exist? The agreement must be that of the associators. When made as the law requires, the articles constitute the constitution of the company. That the law contemplates the articles of association to be made by an agreement, is evident from the 7th paragraph, which provides, "any terms and conditions of membership therein, which the corporators may have agreed upon, and which they may deem important to have set forth in such articles." The law carefully provides against putting in the articles any thing improper, by the provision that they must be submitted to the attorney general, and approved by him.

This law is unusual. Generally, the statute provides for the government of corporations by mandatory provisions. Here, the matter is designedly and explicitly left to the agreement of the corporators, and this offer of the power of agreement is made for the benefit of the corporators to induce them to engage in a proposed enterprise.

Articles of association are generally contracts by the members.

Cook on Stock and Stockholders, Sec. 492.
Zabriskie vs. Hackensack R. R Co., 18 N. J. Eq., 178.
Snook vs. Georgia Improvement Co., 83 Geo., 61.
Morawitz on Corporations, Vol. 1, Sec. 43 and seq.

2. It is uniformly held, that where the charter of a company provides a method of electing directors and there is no reservation of a power to change, the legislature has no power to change such provisions in favor of minority representation. If this is true when the provision is embodied in a contract with the state, it must be more true when the contract is between the corporators.

In *Hays vs. Commonwealth*, 82 Pa. St., 518, a case of a charter where no power of change is reserved, it is held, that a minority representation provision of the state constitution cannot apply, and the court say on page 522, as to this provision, "Now, while it cannot be said that this would not be an alteration in the terms of the charter, it is nevertheless urged that it is a mere regulation of the right of suffrage in corporations, but affects the vested rights of no one. But if it be not a vested right in those who own the major part of the stock of a corporation to elect, if they see proper, every member of the board of directors, then I would like to know what a vested right means. This was

part of the contract under which they entered into the company, and for which they paid their money. The compact was, that they should have the power to select those who should have the management and control of the funds which they had ventured in the enterprise. If, indeed, it be admitted that the minority in a board of directors amounts to nothing, the above stated proposition would not be admissible, but we cannot seriously entertain such an idea, for it was just because a minority does amount to something, and because it can often control or modify the acts of a majority, that the introduction of the constitutional provision under discussion was thought necessary."

The above case is aproved and followed in

Baker's Appeal, 109 Pa. St., 461.
State vs. Greis, 78 Mo., 188.
Smith vs. Atchinson R. R. Co., 64 Fed., 272.

There are no contrary decisions.

II.

No power has been reserved to change the contract of the corporators of the Michigan Mutual Life Insurance Company, as to the method in which the directors are to be elected.

The power is claimed only under the provision of the state constitution, reading thus:

"Corporations may be formed under general laws, but shall not be created by special act except for municipal purposes. All laws passed pursuant to this section may be amended, altered or repealed."

The corporation in question was organized under a

general law, and hence I do not see any limit to the power of alteration or repeal of the law, independent of the reservation. If there is a doubt the reservation clears it away. The legislature can repeal or amend the statute in question just as it can repeal or amend any general law of the state, but no further.

1. The repeal or amendment of the law would not affect the contract between the corporators as to management of their property.

(a) The repeal of the law would only take away their powers to continue the business of insurance as a corporation. Unless forbidden the stockholders could continue the business of life insurance as a partnership. At any rate, they could wind up the business in the name of the corporation, and the method of electing directors would continue as before.

Bewick vs. Alpena Harbor Co., 39 Mich., 700.

(b) Any amendment of the law like an amendment to any other law would not affect lawful contracts entered into before the amendment. The amendment might forbid any new corporations to make agreements except in accordance with the minority representation statute. But surely the power to amend does not cover the power to change pre-existing contracts. This will not be disputed as to contracts made by the corporation with third parties. And I do not see why contracts made by the corporators as to the method in which they shall control their own property on the faith of which they made their investments, should not be held as sacred as any other contracts. It will hardly be claimed that the property of the stockholders in the Michigan Mutual Life Insurance Company, either what was originally put in, or what has been ac-

quired since can be taken away by the legislature. But the control of property is of its very essence. And if the property cannot be taken away neither can its control be changed. If the legislature can change the method chosen by the corporators for the government of the corporation so as to compel minority representation, it can make any other change. It can give the whole control to a minority. It may deprive the majority of the management of the company. When the sacred right of the stockholders to manage their property according to their agreement is taken away, the only further limit is the discretion of the legislature.

It may be claimed that if the legislature can authorize corporators to make unalterable contracts between themselves, the purpose of the constitutional provision under consideration will be defeated. This leads to my next head.

2. The provision in state constitutions authorizing the amendment or repeal of all laws for the formation of corporations, is intended simply to protect the public against corporation monoplies and corporation abuses. It is not designed to affect the contracts of the corporators among themselves as to the control of their interests in the property. There is no more reason why the state should be interested in the contracts of corporators as to the methods in which they may vote their stock, than in the contracts of partners as to the control of their partnership property. The state is not interested in making all contracts, subject to amendment or repeal, at the will of its legislature, and so evading the provision of the constitution of the United States, as to the impairment of the obligation of contracts. Its object is to protect itself against a certain class of contracts, which have been found to constitute a public injury.

The opinion of the Supreme Court of Michigan, (Record, p. 19,) is put on the ground, that the public is interested in the control of a great life insurances company like the Michigan Mutual, that the policy holders are as much interested as the stockholders. This is true, but this interest of the public is provided for by abundant provisions of the act, requiring reports of the condition of the company, and authorizing examinations of the assets by public officers. If these provisions in practice prove insufficient, they may be amended or new provisions added. But surely, the state is not interested in having all the directors elected each year, instead of having them elected in three divisions, each serving for three years. Nor can it make any difference with the public, whether or not a certain minority of the stock may elect one or more directors.

The method of electing directors by a majority vote of all the stock was, until recently, the almost universal one. It was changed, in some states, not because any evil was thought to have resulted to the public from the old method, but in order to favor minorities of a certain size. The public is abundantly protected, if the affairs of a Life Insurance Co. are managed according to law, honestly, and with good judgment. There can be no presumption that the management of a board of directors elected with minority representation will be better than that of one elected in the old way, and certainly the powers of the policy holders are not increased by minority representation of the stockholders.

The question is not whether the legislature of Michigan under the constitution of the state may allow persons about to incorporate to regulate by contract among themselves, the general powers of the corporation, which affect the public, but only whether such power to contract may be given as to the rights of the incorporators among them-

selves. Such power now exists among all unincorporated associations, and no public interest is suffering in consequence.

III.

I have found no cases in conflict with the view I seek to maintain, though there may be some, which appear to be so.

Sherman v. Smith, 1 Black, 587.

A new York bank was organized under a general law subject to amendment and repeal providing that the stockholders should not be personally liable unless they put in their articles a provision for such liability. The bank in question provided in its articles against personal liability, and this was claimed to be a contract within the provisions of the United States constitution. Held that the law did not authorize such a contract, and that putting a provision of the law in the contract, without authority, did not prevent the law from being changed.

Like this last case are *In Re* Lee & Co. Bank, 21 N. Y., 9, and the Reciprocity Bank, 22 N. Y., 9.

The difference between these cases and the one at bar is obvious. In them there was no authority given in the general law for the corporators to make a contract, as to their liability. This was determined by a general law, which like all general laws was liable to change. The question was one which concerned the public, and not merely the control of their own property by the corporators.

In *Close v. Greenwood Cemetery*, 107 U. S., 466, it was held that Congress could change the government of a cemetery association so as to fix the interest of the origi-

nal proprietors and give a large number of lot owners a certain power of control.

The law under which the association was organized did not provide that the original corporators should agree on the power of control, and Congress is not subject to the limitations on the States in the United States constitution. The change made was in the interest of the lot owners, and not of a minority of the stockholders.

Penn. College Cases, 13 Wallace, 190.

Here three colleges were united against the protest of the trustees of one and of a number of persons who had bought scholarships. The union was sustained. The new college was bound by the scholarships given by the old one. The difference between this case and the one at bar is plain. The trustees had no property interest in the old college. They had no agreement as to its management. The whole matter concerned public and not private rights.

Spring Valley Water Works v. Schottler, 110 U. S., 347.

A general law subject to amendment or repeal, gave the power of fixing water rates to a board appointed in part by the corporations, and in part by the municipalities. This was amended, so as to give the power entirely to the municipal authorities. The amendment was held valid. It was considered but a change in the general law, and so within ordinary legislative power.

Greenwood vs. Union Freight Co., 105 U. S., 13.

This was a case where a charter was repealed. It was held, that whatever the legislature gives, when the right of repeal is reserved, it may take away. I have no quarrel with this doctrine, nor with the view that the legislature

may alter any franchise it gives in behalf of the public. Nor do I doubt that the stockholders of a company take all their rights subject to the reserved rights of the legislature to amend or repeal. The whole question at bar is, whether or not the right of amendment reaches to the private right of the stockholders, secured by a lawful agreement among themselves to control the property of the company in a manner which does not concern public interest.

IV.

There is little direct authority in support of my position, but principles have been announced in the cases which cover all I claim.

In *Sage vs. Dullard*, 15 B. Monroe, 340, it was decided that a charter given to a Theological Seminary, providing for its government by a number of trustees, who were authorized to fill vacancies, could not, under the reservation of a power to amend, be changed by the legislature by adding sixteen new trustees. On page 359 there is a good discussion of the principles involved.

Orr vs. Bracken County, 81 Ky., 593.

A plank road company was organized under a charter reserving the right of amendment, which provided for the election of a president, treasurer, and ten directors. The stockholders were not entitled to a vote for each share of stock, but the vote was so regulated as not to give the largest stockholders the right to elect. The legislature amended the charter so as to reduce the number of directors to six, and allow each stockholder a vote for each share of stock. The amendment was held void. The court say,

p. 596: "The right to amend the charter may be expressly reserved, but that right does not confer the power of taking from the corporators the control of the corporate property, or to change the object of the charter by taking from those having a right to select their officers that right and placing it in the hands of those whose stock by reason of the increased power conferred by the amendment are enabled to control the corporation."

Zabriskie vs. The Hackensack R. R. Co., 18 N. J. Eq., 178.

On page 185, the Chancellor, in discussing the reserved power to amend or repeal corporate acts, says: "The object and purpose of these provisions are so plain that it seems strange that any doubt could be raised concerning it. It was a reservation to the state for the benefit of the public to be exercised by the state only. The state was making what had been decided to be a contract, and it reserved the power to change by altering, modifying or repealing the contract. Nejther the words nor the circumstances, nor apparent objects for which the provision was made, can by any fair construction extend to giving a power to one part of the corporators as against the other, which they did not have before."

Snook vs. Georgia Improvement Co., 83 Geo., 61.

On page 85, it is held, "that the charter of a corporation is a contract of a dual character; first, a contract between the state which grants the charter, and the corporation; and second, a contract between the corporation and its members; and while the state, if it reserves the power to do so, can alter and amend the charter, and the corporation itself cannot object to the alteration or amendment, yet,

the state has no power to make any material essential alteration in the contract between the members themselves and the corporation."

Fisher vs. Patton, 33 S. W., 451.

On page 456, it is held, that a contract between a building and loan association, and its stockholders, valid when made, cannot be changed by an act of the legislature.

Detroit vs. Detroit & Howell R. R. Co., 43 Mich 140.
People vs O'Brien, 111 N. Y., 1.

In these cases it is held, after the fullest consideration, that rights in the streets of a city acquired by the exercise of the franchises of a corporation, cannot be taken away by any amendment or repeal, however broad may be the reservations.

Hill vs. Glasgow R. Co., 41 F., 610.

In giving the opinion of the court, Judge Jackson, after quoting from the decisions of this court, says: "The principle of these and other decisions upon the subject of amending or repealing charters under a reservation of power to do so, is that the legislature may change or modify the privileges and franchises which the state has granted the corporation, and which concern the interest of the public, but dealing with what it has bestowed either by way of withdrawal or alteration, the state may not go further and so legislate as to disturb, affect or impair rights either of the corporation or of its shareholders previously acquired while the corporate franchises were being legally exercised. All rights thus acquired of whatever character are surrounded and protected by constitutional sanctions and guarantees higher and superior to the legislative power of amendment or repeal."

Southern Pacific Co. vs. Board of Commissioners, 78 F., 236.

In this case there is citation of the authorities and a discussion of the limits of the power to amend or repeal corporate rights.

Tomlinson vs. Jessup, 15 Wallace, 454.

On page 459, this court, in reference to the power to amend or repeal, say: "The reservation affects the entire relation between the state and the corporation, and places under legislative control all rights, privileges and immunities derived by its charter directly from the state. Rights acquired by third parties, and which have become vested under the charter in the legitimate exercise of its powers, stand on a different footing."

Shields vs. Ohio, 95 U. S., 319.

On page 324 this court say, "The power of alteration and amendment is not without limit. The alterations must be reasonable; they must be made in good faith, and be consistent with the scope and object of the act of incorporation." And again, "Beyond the sphere of reserved powers, the vested rights of property of corporations are surrounded by the same sanctions and are as inviolable as in other cases."

Greenwood vs. Freight Co., 105 U. S., 13.

On page 19 this court say, "In short, whatever power is dependent solely upon the grant of the charter and which could not be exercised by unincorporated private persons under the general laws of the state is abrogated by the repeal of the law which granted these special rights. Personal and real property acquired by the corporation during its lawful existence, rights of contract, or choses in action so acquired, which do not in their nature depend upon the

general powers confered by the charter are not destroyed by such repeal. The rights of the shareholders of such a corporation to their interest in its property are not annihilated by such repeal."

If the law under which the Michigan Mutual was organized had been repealed, I know of no reason why the stockholders might not have continued life insurance as partners. The only limitation of the right to do such business is found in this law. Howell's Statutes, Sect. 4237.

On this repeal the business would have been open to every one. And the management of the business, in the absence of some new agreement, would have been controlled by the agreement in the articles of association.

And if the legislasure could not have taken away by repeal of the act, the power of the stockholders to do business according to their agreement, it would seem certain that no amendments can reach such a result. If the property of the stockholders is preserved in spite of a repeal or any possible amendment, this property must remain under the control of such stockholders. And the manner of control should be that on which the stockholders have agreed.

V.

Another error alleged is that the judgment of the court below deprives respondents and other stockholders of their right to participate in the management of their property, according to their agreement, without due process of law, in violation of the fourteenth amendment. The subject of vested rights in the control of property is so ably argued in three dissenting opinions in the *Sinking*

Fund Cases that I need only to refer to them, 99 U. S., p. 731, *and seq.*

Though the majority of the court did not agree with the dissenting judges in the decision of that case, yet the difference was probably not in the principles advocated but in their application to the case then at bar.

I submit that the judgment of the court below should be reversed.

C. A. KENT,

Of Counsel for Plaintiff in Error.